

***United States Court of Appeals
for the Second Circuit***



**APPELLANT'S
REPLY BRIEF**

77-1140

To Be Argued By
WILLIAM B. LAWLESS

United States Court of Appeals
FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA,
Appellee,
v.

DAVID STIRLING, JR., WILLIAM G. STIRLING,
HAROLD M. YANOWITCH, EDWIN SCHULZ
and RUBEL L. PHILLIPS,

Defendants-Appellants.

REPLY BRIEF OF DEFENDANTS-APPELLANTS DAVID
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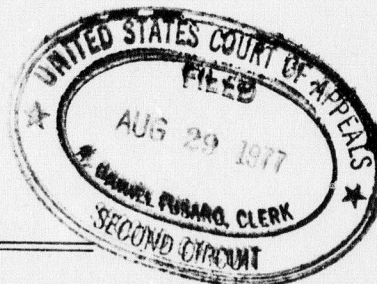




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Abbreviations

References to the Joint Appendix and Exhibit Volumes filed on behalf of defendants-appellants David Stirling, Jr., William G. Stirling and Harold M. Yanowitch are indicated by the letters "A" and "E", followed by the number of the page at which they appear, e.g., "A 423", "E 224".

References to Transcript pages, Government Exhibits, Defendants' Exhibits and defendant Schulz's Exhibits not appearing in the Joint Appendix or Exhibit volumes are indicated by the prefixes "Tr.", "GX", "DX", and "Schulz Ex.", respectively.



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REPLY BRIEF OF APPELLANTS
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Preliminary Statement

For the most part, the Government's statement of facts is more significant for what it omits than for what it contains. Although the Stirlings' initial brief presented a review of the evidence based almost exclusively upon the testimony of the Government's own witnesses, the Government's 50-page review of the case does not once address the stated failures in its own proof. More unfortunately, in avoiding these omissions in its proof, the Government has also substituted its own gloss for the testimony and evidence which it presented at trial.

Thus, in questioning the propriety of certain sales booked to the Virgin Islands project, the Government refers to a telegram from the customer (GX 573) "cancelling those contracts" (GB, p. 39). In fact, the telegram on its face was a transparent attempt to renegotiate the purchase price, and the customer sent Homex's auditors a confirmation of its indebtedness for the full contract price the very next day (GX 252A at 21,840-41). Likewise, the Government repeatedly refers to Homex's press clippings file (GX 166) and attempts to portray defendants as heavily engaged in a four-year publicity campaign on behalf of Homex. In point of fact, there is not a single word of testimony or evidence that either David or William Stirling initiated, made substantive contributions to or stopped any Homex press release.* Similarly, the Government denigrates an independent appraisal performed with respect to the Raseac and Kece Associates parcels (E 393a) by calling it "a friendly appraiser's statement", when there is not a single shred of evidence indicating such relationship between Homex and the appraiser. In the same vein, the Government suggests that Homex switched auditors because of Harris Kerr Foster's ("HKF") auditing requirements (GB, p. 27-28),

*The Government's confusion as to Homex's public relations activity is further indicated by its mistaken assertion that a film was made of the installation of Homex's first modules (GB, pp. 4-5). The film, which showed the installation of the Troupe and Clarissa Streets project, was made at a time when Homex had already manufactured and installed hundreds of modules.

despite the testimony of its own witnesses that Homex was getting contradictory and belated answers from HKF (Tr. 3252-53). With respect to the Clay and Southbridge bookings, the Government totally fails to alert the Court to the fact that none of the unidentified "commercial and investment bankers" who saw these sales reflected in Homex's unaudited interim financial statements claimed that they were deceived (GB, pp. 21-22, 36). Likewise, in suggesting that the defendants were "personally censoring every item of information being supplied" Merrill Lynch's attorneys (GB, p. 27) the Government can point only to a memorandum in which defendants proposed to permit inspection, but deny them copies, of sales contracts (E 485-90). A more candid appraisal of defendants' intent would include a citation to the subsequent memorandum which recited that the attorneys had been given copies of those contracts and anything else that they requested (GX 630 at 64,427).

It is not the function of this reply brief to respond to each and every distortion and misstatement contained in the Government's brief. However, in responding to the issues raised on this appeal, we would ask the Court to review carefully the evidence cited by the Government before accepting its characterizations as either fair or accurate.* We would further ask the Court to note that, without explanation, the

*We acknowledge that this task may not be simple, since the Government's citations to the record are often palpably incorrect, even to the extent of citing a court reporter's index page for a disputed factual assertion (GB, p. 18 ["Tr. 3109"]).

Government's orientation on this appeal has markedly shifted from the case it tried below.

At trial, the Government did not contend that defendants had derived "considerable financial advantage" from their involvement with Homex (GB, p. 3); indeed, the Government stipulated that every dollar the Stirling brothers received from the sale of their stock had been in return for the assets which they had contributed to the corporation (3955). Likewise, the jury never heard "that from beginning to end [Homex] was a massive fraud conceived and executed by defendants" (GB, p. 3). To the contrary, the Government essentially conceded that there are thousands of families living today in homes designed, manufactured and installed by Homex (Tr. 5949-50). The simple facts are that the Stirling brothers were self-made millionaires before they ever went into Homex, they introduced a revolutionary and socially useful product to the American market, and, with the best legal and accounting advice that Wall Street could provide them, managed to come out financially ruined five years later.

The Land Transactions

Although the specifications involved in each of the Raseac, Kece and 57 & 31 transactions differed in certain material respects, the proof offered by the Government at trial as to each of them had certain common characteristics. The proceeds of these sales were never represented in Homex's SEC filings as anything other than extraordinary income items, with the caveat

that "the Company does not anticipate that land sales will be a significant part of its business in the future" (E 10 [GX 1]; E 51 [GX 5]; E 87 [GX 8]; GX 10 at 8).^{*} Likewise, Homex never represented that these sales were cash transactions, and indeed made full disclosure of the deferred aspect of each sale in the footnotes to the financial statements (E 23 [GX 1]; E 67 [GX 5]; E 107 [GX 8]; E 158 [GX 12]; E 226 [GX 16]). Moreover, the evidence below indicated, without any contradiction, that the sale price for each parcel represented the fair market value of the land. Finally, it is most significant that not one of the Government's witnesses testified that the so-called "guarantees" were or were thought to be enforceable against the individual giving that guarantee, and several of these witnesses affirmatively stated that no "guarantee", enforceable or otherwise, was ever extended on behalf of Homex itself. See, e.g., A 221, 230, 252; Tr. 1194-95.

It is not surprising that, given these facts, the Government's case against defendants quickly reduced itself to the issue of the "side promises" allegedly incident to these transactions, the alleged non-disclosure of critical facts to Homex's auditors, and the fact that in each case the purchasers of the property were shell corporations. Since the Government has apparently discovered since trial that undeveloped real property is usually purchased through shell corporations, we shall confine

^{*}For some reason, the Government never quotes or refers to this caveat.

our reply to the alleged side agreements -- as revealed by the testimony of the Government's own witnesses -- and the alleged misrepresentations made to Homex's auditors.

(a) Kece Associates

The Government's contentions with respect to the Kece transaction essentially reduces itself to two claims: that the sale was really an option contingent upon the further separate sale, at an undetermined price, of 330 modules; and that the defendant David Stirling "covered up" Kece's default by securing payment of the arrears without any expenditure of funds by Homex.* Logically, there is little to commend either of these arguments; however, since the record cited by the Government simply fails to support either of these claims, we need not inquire into whether a completed sale can really be an option or a paid-up mortgage is truly a default.

The "option" argument hinges upon the fact that after the deal had been closed and the deed recorded in the County Clerk's office, Homex sent a letter to Kece agreeing to sell it 330 modules -- which had not yet been designed, manufactured or priced -- within the next two years "at Homex's then published prices." (E 380) On its part, Kece warranted that "to the extent they are available . . . Homex modules will be used

*During the trial, the Government had also contended that the disclosure of the transaction in SEC filings was inadequate because the sale was at a falsely inflated price and because Kece was a shell corporation. While these arguments no doubt impressed (if not confused) the jury in counsel's closing argument (Tr. 5554-56), the Government has wisely abstained from bringing them before this Court.

exclusively for the construction of the apartments". (Ibid.)* Significantly, the letter of intent in no way conditions Kece's obligations under the separate contract for the sale of the land (GX 73). Moreover, the so-called "package price for land and modules" which the Government posits (GB, p. 9) is hardly a bargain basement prize: the modules were to be sold to Kece at published prices, which, given both the expected quantity of production for non-Kece use and the relative cost of 330 modules (probably in the area of \$6 million) to the \$302,000 Kece receivable, would not be affected one whit by the possibility that Thun would walk away from the Kece mortgage if the price did not suit him.

The Government attempts to sidestep the plain text of the letter of intent by quoting Thun's statement that, as structured, the transaction "had more the characteristics of an option on the land" (GB, p. 9, citing Tr. 3094) and suggesting that David Stirling shared that "understanding". Unfortunately, this argument ignores Thun's own testimony that the transaction, even with its "characteristics", was "an absolute outright purchase" of a piece of property that, with or without modules, was a very smart investment: its appraised value was \$310,000 (against a total purchase price of \$325,000); it abutted on a Thun development in which he had already invested seven million

*Of course, the fact that Thun, to get even this nebulous commitment, was willing to grant Homex an exclusive right to sell its 330 modules only underscores the incredible demand for Homex's products throughout 1969 and 1970.

dollars; and it could have been developed with conventional housing just as easily as with Homex modules (A 384, 393-94; E 382; Tr. 3103). Indeed, the desirability of this parcel to Thun was so obvious that, long before the transaction, Thun had bargained for a right of first refusal on it lest it fall into someone else's hands (A 392, 394).

The balance of the Government's case relates to the October 1970 and February 1971 payments which Thun made on the Kece mortgage, which were allegedly induced by the Stirlings' sales to Thun of their interest in various joint ventures in which they had been co-venturers (GB, pp. 21, 31). The assertion that these transactions were related is totally unsupported by Thun's own testimony, since he recalled that the closings in which these payments were made covered a wide variety of transactions (compare Tr. 2217-23 [cited by Government] with Tr. 3179-80), and that, had the Stirlings remained in the limited partnerships, they would have been personally liable for more than a million dollars which these partnerships were borrowing (Tr. 3134, 3172-73; cf. Tr. 3119-20). Indeed, the Government's account of the Thun-Stirling transactions blithely ignores the fact that in the years prior to these payments, the Stirling brothers and Thun had entered into transactions between themselves involving approximately twenty million dollars in real estate investments (Tr. 3139). Of course, not one nickel of Homex's funds were paid, or even alleged to have been paid, to secure Thun's payments on the alleged \$325,000

"option" on the property abutting his seven million dollar residential development.*

(b) 57 & 31 Development Corporation

The deficiency in the Government's presentation of the 57 & 31 transaction proceeds from the same omission in its proof which were pointed out in the Stirling's initial brief. Although the alleged "side promise" was the diversion of work to Empire Pipeline in return for its principals having entered into the transaction (GB, p. 23), the Government has not pointed to even a single project which was given to Empire Pipeline after the transaction was finalized. Similarly, the Government suggests that David Stirling "arranged" the \$250,000 bank loan to 57 & 31 from the First National Bank by depositing \$100,000 of Homex funds at that bank, without mentioning that the deposit was returnable on demand (Tr. 2115). Likewise, the Government conveniently fails to mention that the 57 & 31 principals personally guaranteed the First National loan, and that their own net worth was almost a million dollars -- four times the amount of the First National loan (A 265-66; E 378-79, 394-406). In addition, the Government understandably downplays the fact that Homex -- despite the approval of the transaction as a sale by Peat, Marwick ("PMM") -- excluded the transaction from sales before the final Merrill Lynch prospectus was

*Likewise, the allegation that the Stirlings "had themselves made the recent payment on Kece's behalf" (GB, p. 21) is not supported by its citations to the record.

filed.

To be sure, most of the Government's case on 57 & 31 is based on artistic license, not the testimony of its witnesses. Thus, in suggesting that David Stirling countered "Wynn's response . . . that such a deal was simply out of his and Grago's financial league . . . by dangling the prospect of sufficient additional Homex 'developmental work' to Empire . . . (Tr. 985-86)" (GB, p. 21), the Government relies solely upon Wynn's testimony that:

"I wasn't sure we could handle that magnitude of a project financially.

"And David then explained to me that he felt that there wouldn't be any substantial tie-up of cash or risk involved in the project because of the surrounding development work that was going to occur there and the amount of work that we would be performing on their behalf through our construction activities, and that he felt we would be able to carry the project.

"Q. Do you recall anything further in that regard?

"A. Well, we discussed the relative value of the property, and I agreed with him that the \$2.1 million did represent the going prime value of that type of property as it was in that area." (A 235).

Significantly, neither Wynn nor Grago ever testified to any promise of additional Homex work beyond that which they were already doing, and neither they nor anyone else attributed the "surrounding development work" to a future Homex project. The alleged "guarantee" was equally nebulous: as in the case of Raseac, David Stirling is quoted as having said that Wynn and Grago "would not be hurt" at the same time that he emphatically

disclaimed any guarantee from Homex (A 256-57).

The balance of the Government's claim relates to the alleged failure to disclose "First National Bank's loan to route 57 & 31 or the inducements and security for it." (GB, pp. 24, 30).^{*} Understandably, the Government's recitation of the facts does not claim that any of the defendants were ever asked about these matters by the auditors or that they ever instructed any of the former Homex executives who testified as Government witnesses to withhold such information from the auditors.^{**} Indeed, the Government's confusion about defendants' role in the disclosure of this transaction is further indicated by its assertion that the Homex response to the SEC's comment letter was "prepared by Schulz and Yanowitch, in collaboration with PMM" -- despite Murray's testimony that the part of that document relating to 57 & 31 was written verbatim by him alone (Tr. 3299-3300).

^{*}The "security" referred to consists of the assignment of the condemnation award to First National, the significance of which was never called to defendants' attention by the experts who audited Homex. It is interesting to note that, although both Murray and Mauriello testified at length about their discussions of this transaction with Davis and Yanowitch, neither of them claimed to have asked how 57 & 31 secured its financing. Given the fact that its principals had personally guaranteed the indebtedness and had a net worth of almost \$1 million, the inquiry would have been pointless.

^{**}Thus, Reuben Davis, a former Homex officer, who had authored the letter assigning the condemnation award to First National (GX 61), testified that he himself had described the transaction to Mauriello (Tr. 1267-68). Since Davis, a Government witness, never testified that Yanowitch or anyone else asked him to withhold any information from Mauriello or PMM, the Government's suggestion of a wilful non-disclosure is unsupported by the record.

Essentially, the 57 & 31 part of the Government's case is constructed from the misrepresentation of the alleged "side promise", the wilful omission of the personal guarantees which secured the bank loan, and an approach to the evidence which can most charitably be characterized as fast and loose.

(c) Raseac Realty

The Government's presentation of the Raseac transaction is discussed in the Yanowitch Reply Brief ("YRB") at pp. 4-8.

David Stirling's involvement in this transaction centers around his alleged "direct role in the fabrication of the original transaction" (GB, p. 64), which essentially consists of his ratification of oral representations previously made by Yanowitch. Significantly, the Government totally ignores the testimony of its immunized witness, Bernard Frank, that Yanowitch had claimed that he was being "really criticis[ed by his superiors] because here he had put together a deal with responsible businessmen a year, a year and a half ago and it was falling apart . . ." (A 272). This statement hardly lends support to any belief by the Stirlings that Raseac was a sham transaction, and the record itself is barren of any participation in the statements made to Homex's auditors relating to this transaction.*

*The Government suggests that David Stirling had "actual knowledge of the SEC's ASR No. 95 concerning land sales", although this assertion -- made with respect to a high school drop out -- is not supported by the testimony cited (GB, p. 64).

Stock Purchases for Union Officials

By far the largest portion of the Government's statement of its evidence is devoted to the claim that the Stirlings and Yanowitch bribed union officials to secure special advantages for Homex, and that purchasers of Homex stock were materially misled because the company did not disclose these payments in its SEC filings. Unfortunately, the Government's position essentially presumes the two facts which were most notably absent in the evidence below: that Homex secured any favored treatment from the United Brotherhood of Carpenters and Joiners of America ("UBCJA"), and that any reasonable investor could rely upon SEC filings which uniformly refused to assure any continuation of harmonious labor relations.

Even if it be assumed that Homex received special undisclosed benefits from the UBCJA, it is difficult to perceive how a shareholder can rely upon a statement in the Merrill Lynch prospectus that the UBCJA contract was to expire in less than two months and that the company "can give no assurance" that ensuing negotiations would be without difficulty (E 135). To the extent that the Government addresses this fact at all, it mistakenly argues that "defendants wisely do not make a claim that [the loans to union officials] were in fact immaterial", and then proceeds to spend the balance of a 700-word footnote claiming waiver and, in passing, materiality (GB, pp. 88-89n).*

*The materiality of the transactions involving UBCJA officials, alleged in paragraph 16 of the indictment, was raised by a motion to strike prior to trial, and is further discussed at pp. 22-27, infra.

Indeed, in searching for some representation of continued labor harmony, the Government presents this Court with a 1970 press release issued by Sanders, Stiver & Co., a Cleveland broker-dealer (GB, p. 18). The manner in which the Government uses this release is more misleading than anything in the release itself: no connection was ever shown between anyone at Homex and the preparation of the release; the Government never called a witness from Sanders, Stiver to testify about its preparation; and the sole pretext for its being in evidence was its inclusion in the public relations department's file of press clippings (GX 166).

More importantly, the Government's exhaustive "treatment" of this part of the case ignores the fact that every UBCJA official who took the stand claimed that neither he nor any other official ever gave Homex special treatment (A 192, 202; Tr. 598-99, 603-05, 616, 636). Even the Government's star rebuttal witness, Theodore Kheel, testified that Homex dealt at arms-length with the UBCJA (Tr. 5384-85). In fact, the Government does not cite even a single word of testimony to support the suggestion that Homex got special treatment.

Instead, the Government points to Ruggiano's weekly reports to the International (GX 734), and suggests that the UBCJA agreement with Homex was a deviation from "normal practice" intended to exclude the United Auto Workers (GB, p. 5) -- a claim squarely denied by both Kheel and Ruggiano (Tr. 598-99,

5398).* Similarly, Ruggiano and Jacobs' appearances at the Akron City Council Planning Commission were standard operating procedure for construction unions, which -- as indicated by the part of the Ruggiano memorandum not quoted at page 6 of the Government's brief -- were intended to prevent members (as Ruggiano noted, 500 in Akron alone) from losing their jobs because of administrative red tape and local politics (GX 734 at 12/7/68). Both Ruggiano and Jacobs testified that their participation before these boards were perfectly proper (A 191; Tr. 656). Furthermore, since the last of these activities occurred in November 1968, it is difficult to perceive how they could have been influenced by stock which was not purchased until March 1970.**

The most curious aspect of the Government's claim of preferential treatment is that its posture in the brief wholly ignores the fact that no evidence was introduced to show any

*Since the UAW would certainly not have had jurisdiction over Homex's job sites, it is difficult to perceive why they should have been competing with the UBCJA for representation. Apparently, the Government's claim is an afterthought, since the record is devoid of any protest or complaint by the UAW.

**The only post-purchase activity attributed to Ruggiano is that he "forcefully settled disputes", including "on terms violative of the second June 1969 Homex contract with the UBCJA", in the latter part of 1970 (GB, pp. 18-19). We invite the Court to check the Government's references to the cited exhibits, since we can find absolutely no support in them for the proposition that Homex received such special attention from Ruggiano. Significantly, the Government did not even attempt to elicit testimony from Ruggiano to support such characterizations.

deviation by the UBCJA from its normal practices and procedures. It is most surprising that the Government points to the stock interest of UBCJA officials who disclaimed ever having known that they owned Homex stock, while ignoring the ownership and loans to Homex's production-line employees (Tr. 633-34, 678, 699-700). Indeed, if anyone in Homex's labor relations were influenced by ownership of its stock, it was probably the hundreds of Homex factory workers who were able to buy stock at the original issue price, many of whom financed these purchases with loans from banks which had been arranged by Homex or funds loaned to them by Homex itself (A 192; Tr. 1743-49).

The balance of the Government's recitation of the evidence largely consists of a series of red herrings. While referring to Dienstag's "perceived fiduciary obligation" which led him to recommend against putting public and union officials on Homex's initial offering list (GB, pp. 14-15), the Government fails to note that Dienstag's answer was based on possibly adverse public relations (GX 719 at 81,612); Homex's outside SEC counsel said that the legality of such inclusion under federal law was an open question (GX 719 at 81,613); and, in point of fact, no UBCJA officials were included on the original issue list (Tr. 376).*

Similarly, in describing Ruggiano's having been "assured . . . that Yanowitch had checked it out and that everything

*Significantly, Dienstag, as Homex's in-house SEC expert, made absolutely no mention of the possibility that such a benefit would have to be included in Homex's SEC filings.

was 'perfectly legal'" (GB, p.7), the Government misstates Riggiano's testimony, which was that David Stirling said "it" was legal and that he would check with Yanowitch (Tr. 581-582). Ruggiano himself never spoke with Yanowitch and, since he testified that he did speak to an attorney before purchasing Homex stock, it was probably Harold Cohen, an attorney representing the UBCJA, who had suggested to Catalfano, another UBCJA official, that he buy Homex stock (Tr. 580, 695-97). Moreover, the Government has yet to explain what "it" referred to -- owning Homex stock or getting on the original issue list.

Likewise, the Government's reference to defendants' "discussions and plan" to include UBCJA officials on the original issue list (GB, p. 16) posits conversations which were educed and highly unlikely -- Langone himself testified that David Stirling immediately dropped their names from the list when Langone said it would not be "appropriate" (A 175-76). In the same manner, the Government's brief recitation of Theodore Kheel's rebuttal testimony -- "that at no point during his association with Homex was he advised that the seven UBCJA officials had been proposed and then included as purchasers of Homex stock" (GB, p. 50) -- fails to mention the trial court's exclusion -- at the Government's insistence -- of an eighth UBCJA official, Peter Turzik, who would have testified that Kheel himself had put him into Homex. See pp. 42-43, infra.

Mississippi Sales

The Government's contentions with respect to the Greater Gulf transaction are more fully reviewed in the Yanowitch Reply Brief at pp. 10-13.

The Government's attempt to impute knowledge of the alleged forgery of the \$15 million commitment letter to the Stirlings rests solely upon Marshall's testimony that David Stirling and Yanowitch told him "not to leave that letter" with Chemical Bank (A 329). Putting aside the fact that Marshall's contemporaneous memorandum of that visit does not refer to any such request from either Stirling or Yanowitch (GX 990 at 69,867-68), Marshall did in fact permit Chemical to make a copy of the letter (A 330). It is highly unlikely that Yanowitch or anyone else would treat a document with "promised secrecy" (GB, p. 29) by permitting it to be copied.

Accounting Practices

The Government's assertions with respect to the allegations in paragraphs 13 and 15 of the indictment (A 15-16) are discussed in Yanowitch's Reply Brief at pp. 13-17, which is incorporated by reference herein.

The Government's case against David Stirling with respect to these accounting matters basically relies upon its own omissions and misstatements.* The mere reassignment of modules from one contract to another was never claimed to be misleading, except to the extent that PMM was not aware of it when it certified the financial statements to the Merrill Lynch prospectus. Yet PMM's own work papers -- edited for purposes of its civil litigation (Tr. 4823-26) -- indicated that it was aware of the practice no later than March 1971, and, if there ever was any accounting reason to question the propriety of such practice, such advice was apparently never given to either Schulz or David Stirling (Tr. 4790, 4798). Moreover, the Government's suggestion that David Stirling himself was personally involved in making the reassignment decisions (GB, p. 65) is belied by the testimony it cites.

With respect to the 1970 cost overruns (Indictment, ¶15[a]), the Government overlooks Schulz' concession that he never told the other defendants about the "Christman incident" (Schulz Brief, p. 20), and principally relies upon a subsequent memorandum from Schulz to David Stirling stating that the overruns "should not be discussed with [PMM] since it could tend to indicate our uncertainty as to [collection]." (GB, p. 66n, quoting GX 817 at 90,399). A more candid appraisal

*The Government concedes that William Stirling was not involved in this aspect of the case (GB, p. 91).

of that memorandum would have included the fact that it was written before the receipt of the HUD letters and that the reason for "not discussing" this was that PMM had not been retained.

The Government presents no evidence linking David Stirling to the U.S. Shelter fee for the Greater Gulf financing (Indicment, ¶15[b]), claiming instead that he "concedes sufficiency" as to that matter (GB, p. 66). This is a gross misstatement of Stirling's contention that the inclusion of the fee in Homex's earnings was not only improper if he actually knew, at the time of its inclusion, that the Farmers Home Adminsitration letter was a forgery. The Government's evidence on that issue was so inconclusive as to warrant the withdrawal of paragraph 15(b) from the jury.

Finally, the capitalization of the Mississippi plant expenses (Indicment, ¶15[c]) was approved by Murray himself, who also testified at trial that this was entirely proper (A 420, Tr. 3293-94). Since Murray never testified that these costs would have been listed as "contingent assets" in the absence of a provision for a reimbursement by a government authority, there was nothing misleading about David Stirling's execution of PMM's audit representation letter.

Argument

I

THE TRIAL COURT ERRED BY PERMITTING THE
JURY TO CONSIDER THE ALLEGATIONS AND
EVIDENCE RELATING TO STOCK PURCHASES FOR
UBCJA OFFICIALS

(Replying to Point II of the Government's Brief)

The defendants have contended, without any refutation from the Government, that Homex's SEC filings disclaimed any permanency of satisfactory labor relations; that no evidence was introduced that the existing labor relations were dependent upon or even affected by the ownership of stock by UBCJA officials; and that, in the circumstances of this case, the disclosure of such purchases in the Merrill Lynch registration statement would have subjected defendants to criminal prosecution.* The arguments advanced by the Government in defense of the trial court's retention of paragraph 16 of the indictment are simply not responsive to the issues raised.

*Defendants David Stirling and Yanowitch also claim that, inasmuch as the only thing which the Government proved was "the purchase and sale of stock for union leaders" (GB, p. 84) -- a violation of the Taft-Hartley Act -- they have essentially been punished twice for the same offense. The Government correctly notes that, in their FRCrP 7(d) motion, defendants stated that they did not claim double jeopardy (GB, p. 84n). However, the Government pointedly fails to consider that David Stirling and Yanowitch are not claiming double jeopardy at the time of their indictment, but by reason of the Government's failure at trial to prove anything more than the facts upon which the Taft-Hartley convictions were based. In effect, the Government's failure to prove either materiality or intent to defraud in connection with this specification results in a deprivation of these defendants' right not to be punished twice for the same offense. It was on this basis that David Stirling's counsel had unsuccessfully moved for a mistrial (A 464; see A 459-68).

The Lack of Materiality

The Government's position with respect to materiality is essentially that "defendants wisely do not make [that] claim in this appeal"; that they have waived that claim "under the principles" of the first rehearing in United States v. Natelli, 527 F.2d 311, 327 (2d Cir. 1975); and, finally, that the fact of the purchases of stock for union officials was material (GB, pp. 88-89 fn.).

The first claim is simply spurious since both the Stirling brothers and Yanowitch raised this argument in their initial briefs (St. Br., p. 36; Y.Br., p. 43). Similarly, the Government's assertion that the Natelli decision bars such argument is equally hopeless in light of this Court's decision on the second petition for rehearing (527 F.2d at 328-29).*

The balance of the Government's argument is the assertion that the purchases of stock for UBCJA officials was a material fact, despite the facts that no UBCJA official claimed that he had ever suggested that Homex receive special treatment, and Homex never gave any assurance of harmonious labor relations.**

*This Court held that Scansarola had preserved his objection to the sufficiency of the evidence on a particular specification by "mak[ing] it sufficiently clear to the trial judge that he wanted a judgment of acquittal or some equivalent" with respect to that issue. In the present case, defendants had questioned the materiality of paragraph 16 by their pre-trial motion, and the district judge's determination of that issue had made further reargument pointless. See Tr. 10/1/76 at 62-63.

**As factual support for the materiality of the purchases, the Government relies exclusively upon Dienstag's memo to Yanowitch -- never transmitted to the Stirlings -- which advised against making stock available to governmental and union officials at the

(Footnote continued on following page)

The fatal weakness of the Government's argument is indicated by the authority upon which it relies, and is further confirmed by the SEC's public pronouncements on "materiality" at the time of these filings.

The legal authorities cited by the Government in claiming materiality do not provide any precedent for such a finding in this case. Thus, in United States v. Bruce, 488 F.2d 1224 (5th Cir. 1973), cert. denied 419 U.S. 825 (1974), an investment company had "bribed certain Labor Union officials to invest union pension funds in [its] investment certificates in violation of federal law", and had used that investment as "a selling point in some of the Company's promotional material" (488 F.2d at 1228). This type of conduct, which did not involve any possible labor unrest, hardly speaks to the present case. Likewise, in In re Central Specialty, 10 S.E.C. 1094 (1942), a company in the midst of a massive dispute over union recognition had filed a registration statement attesting to "very satisfactory [labor relations] in the past", and within two weeks of its effective date the union

(Footnote continued from preceding page)

initial public offering because of "the effect on the company's public image" (GX 719). However, the Government fails to note that this advice was followed. Furthermore, it is significant that Dienstag, as Homex's in-house SEC expert, made no suggestion that such allocations would have to be disclosed. Moreover, when David Stirling asked Langone -- who shared Dienstag's reservations about putting union officials on the original issue list (A 175-76) -- whether it would be proper to purchase Homex stock for UBCJA officials in the aftermarket, Langone told him that it would be proper (Tr. 296-97). There is simply no evidence to support the claim that defendants were aware of the materiality of stock purchases.

had called a strike. The Commission found that, at the time of the filing, "a labor controversy was in progress which might well terminate in a strike" (10 S.E.C. at 1098). In the present case, the Merrill Lynch prospectus specifically noted the incipient expiration of the UBCJA contract and the lack of any assurance of the continuation of satisfactory labor relations, and the evidence did not show any connection between the UBCJA officials' stock ownership and Homex's previous labor relations.* The latter fact is especially significant by reason of the Government's citation of Cooke v. Teleprompter Corp., 334 F.Supp. 467 (S.D.N.Y. 1971), where the omitted material fact was the conviction of Teleprompter's chief executive officer for bribing municipal officials to obtain a CATV franchise, which subjected the company to revocation of its FCC licenses. Not one witness claimed, in marked contrast to the Cooke case, that Homex's relations with the UBCJA were anything other than at arm's length.**

Furthermore, the Government's assumption of the per se materiality of payment to union officials ignores the fact

*Indeed, the bulk of the alleged "good deeds" which the Government points to -- without any testimony to support it -- occurred more than a year before Homex went public.

**The remaining decisions cited by the Government as "cases finding material facts affecting the integrity of management" concern the non-disclosure of self-dealing in corporate assets, a claim that was not raised in this case. Indeed, under New York law, it has been held that the payment of funds to union officials may, in the face of extortion, be a proper corporate act. See Hornstein v. Paramount Pictures, 37 N.Y.S.2d 404 (Sup. Ct. N.Y. Co. 1942) (n.o.r.), aff'd 266 App. Div. 659, 41 N.Y.S.2d 210 (1st Dep't 1943), aff'd 292 N.Y. 468 (1944).

that, when the Merrill Lynch prospectus was filed in July 1971, the SEC's position with respect to materiality did not encompass this type of conduct. Indeed, almost three years later, the SEC was still taking the position that while a conviction for illegal contributions to a political campaign was a material fact, the "disclosure of campaign contributions that may be illegal but have not yet become the subject of a formal proceeding" could be left to the discretion of management. See SEC Securities Act Release No. 5466, [1973-74 Transfer Binder] CCH Fed. Sec. L. Rep. ¶79,699 (March 8, 1974). Even as late as 1975, the SEC rejected the argument that "investors are at least entitled to information regarding matters which embody fundamental national social principles as reflected in federal legislation or court decisions", and stated that the existence of a statutory framework prohibiting certain types of corporate conduct did not mandate disclosure of the corporation's failure to comply with those statutes. See SEC Securities Act Release No. 5627, [1975-76 Transfer Binder] CCH Fed. Sec. L. Rep. ¶80,310 (October 14, 1975). Significantly, one of the items rejected as a per se subject of disclosure was "compliance with the Fair Labor Standards, Occupational Safety and Health and National Labor Relations Acts." Id. at 85,724, n. 72. Indeed, one commentator noted that even as late as last year, the SEC's position with respect to the bribery of foreign and domestic government officials was to do "little beyond encouraging companies to participate in its voluntary compliance program and bringing

enforcement actions against selected defendants with the reasonable expectation of eventual consent decrees." Lowenfels, Questionable Corporate Payments and the Federal Securities Laws, 51 N.Y.U. L. Rev. 1, 21 (1976).

The SEC's first unequivocal statement that it considered the bribery of public officials subject to a standard of per se materiality did not occur until May, 1976 -- five years after the Merrill Lynch prospectus -- in its submission to the Senate Banking, Housing and Urban Affairs Committee investigating "Questionable Corporate Payments". Others have noted that this shift in the SEC's position was a very sharp break with its past pronouncements. See Note, Disclosure of Corporate Payments and Practices : Conduct Regulation Through the Federal Securities Laws, 43 Brooklyn L. Rev. 681 (1977).*

The Government, with the benefit of hindsight, is essentially arguing that in 1971 defendants should have disclosed payments which the SEC itself did not characterize as material until 1976. Additionally, the Government is evading the further question posed in defendants' initial brief -- would the disclosure of the alleged "pay-offs", in the absence

*Indeed, it would appear that the per se test for such payments is far more stringent than the Bar's concept of "materiality". In response to a hypothetical question involving pay-offs to foreign officials, 70% of the members of the ABA Section of Corporation, Banking and Business Law polled stated that such information would have no material effect upon their investment decision. An even higher percentage stated that such information would have no material effect upon the investment decisions "of most other persons you consider to be 'average prudent investors'". See Mann, Watergate to Bananagate: Why Lies Beyond?, 31 Bus. Lawyer 1663, 1665 n. 10 (1976).

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the defendants did not have an intent to defraud, turn upon whether "some of the important information is withheld and not disclosed" rather than upon whether such information was intentionally withheld, that is--was not disclosed notwithstanding an awareness that its disclosure was required. As already noted in defendants' main briefs (St. Br. 420; Y. Br. 49), the clear implication of this Court's decision in United States v. Crosby, 294 F.2d 928 (1961), cert. denied sub nom. Mittelman v. United States, 368 U.S. 984 (1962) is to the contrary. The only case dealing directly with the point which has been found is In re Soroko, 34 F.Supp. 825 (S.D.N.Y. 1940), cited by the Government as authority for its point of view, but in fact diametrically opposed to it.* In that case, the district court had considered a bankrupt's right to a discharge where he had omitted from his schedule of assets a claim against his brother-in-law which the bankrupt's attorney had advised him need not be listed because barred by limitations. The Court held that:

"The referee reports that, assuming the testimony of the attorney to be true, the bankrupt did not fully or fairly set forth to him the facts from which the attorney could advise him whether his claim against his brother-in-law was barred by the statute of limitations and that the fact that this failure by the bankrupt may have been due to the failure of the attorney to elicit this information

*All of the other cases cited by the Government, except United States v. Tolkow, 532 F.2d 853 (2nd Cir. 1976) are discussed in the preceding text and need not be further distinguished in this note. In the Tolkow case, the point now argued by defendants Stirling and Yanowitch was not argued, and reliance was considered only in relation to sufficiency of the evidence and not in relation to what instructions should be given to the jury.

of any evidence of special consideration from the UBCJA, have been more misleading than their omission? Given the fact that every Homex filing emphasized that no assurance could be given as to the continuation of satisfactory labor relations, the inclusion of the disclosure would have implied that there was a basis for expecting continued satisfactory labor relations and thus induced a false sense of security in the permanency of Homex's labor peace.

Violation of Defendants' Privilege
Against Self-Incrimination

In responding to defendants' claim that their prosecution for failing to disclose payments in violation of the Taft-Hartley Act violated the Fifth Amendment, the Government contends that the decisions in California v. Byers, 402 U.S. 424 (1971) and S.E.C. v. Radio Hill Mines Co. Ltd., 479 F.2d 4 (2d Cir. 1973) render the Marchetti- Grosso line of cases inapplicable to this case.* Unfortunately the Government misreads both the Byers and Radio Hill Mines decisions in arriving at its conclusion.

The Byers decision involved the California hit-and-run statute, which required only the disclosure of the driver's name and address (402 U.S. at 432). The Court noted that the defendant's Fifth Amendment claim "Inevitably . . . must be resolved in terms of balancing the public need on the one hand,

*Marchetti v. United States, 390 U.S. 39 (1968); Grosso v. United States, 390 U.S. 62 (1968).

and the individual claim to constitutional protections on the other." (402 U.S. at 427). On balance, the Court held that the statute did not violate the privilege against self-incrimination -- because it was not a criminal offense to be involved in an accident, there was no "substantial risk of self-incrimination", and the disclosure of the driver's name and address was "an essentially neutral act". (402 U.S. at 431, 434). Significantly, the Court suggested that if anything beyond the mere disclosure of the driver's name and address were required, the statute might have been declared unconstitutional. See 402 U.S. at 432, n. 6.

In essence, the Government contends that the balancing test applied in Byers is dispositive of defendants' Fifth Amendment claim. This argument ignores the obvious distinction between disclosing one's name and address -- "an essentially neutral act" -- and disclosing bribery of union officials in violation of the Taft-Hartley Act and the criminal statutes of almost every state, and the palpably greater risk to a defendant who, by disclosing such bribery, concedes his crime, than that of a motorist who, without conceding even civil liability, states that he was involved in an accident. Moreover, the Government's argument ignores the distinction between a disclosure statute, as involved in this case, and the regulatory statute involved in the Byers decision. In that latter instance, the statement is essential to secure the purposes of the statute -- if Byers had held the California statute unconstitutional, the Court was

faced with the prospect of the greatly increased number of motorists who would "stonewall it" by not stopping at the scene of the accident. In the present case, the information withheld is not central to the purposes of the securities statutes -- importantly, there is no specific rule or regulation requiring the disclosure of such payments -- and the particular matter involved, bribery, is exhaustively covered and condemned by an extensive pattern of federal and state laws.

The defendants are not claiming, as the Government pretends, that "any fraud or misrepresentation would be constitutionally protected if the true facts are criminal" (GB, p. 81). In this case, the alleged non-disclosure occurred as to matters which were not specifically required by the statute involved, and which, as of 1971, were not generally considered to come within the general interpretation of materiality. Furthermore, the particular non-disclosure does not fit the "link in the chain of guilt" analysis employed in Byers, where it was too distant, or in Marchetti, where it close enough to be unconstitutional.* In this case, the disclosure sought would, standing

*Indeed, even if the facts had been material, the failure to disclose such facts would have appeared to be protected by the Marchetti and Grosso decisions. Mr. Justice Harlan's concurring opinion in Byers v. California, supra -- announced after the initial Merrill Lynch prospectus had been filed -- pointedly stated that the existing Supreme Court decisions "suggest[ed] the conclusion that the applicability of the privilege depends exclusively on a determination that, from the individual's point of view, there are 'real' and not 'imaginary' risks of self-incrimination" (402 U.S. at 437).

alone, be enough for conviction under the Taft-Hartley Act by the same government which required the disclosure.

The Government's reference to this Court's decision in SEC v. Radio Hill Mines Co., Ltd., supra, fails to resolve the differences between this case and Byers v. California, supra. The reporting provision which the Court upheld was the disclosure of Stein's beneficial and record ownership of securities, which was "generally or completely 'lawful activity', and disclosure of such ownership is not an admission of an 'inherently suspect' activity." 479 F.2d at 7 [citations omitted]. No one has ever claimed that the purchase of stock for union officials is lawful, and it certainly is "inherently suspect" inasmuch as it is specifically prohibited by the Taft-Hartley Act.

As its final argument, the Government contends that even if the disclosure was protected by the privilege against self-incrimination, that privilege was waived because it was not claimed in the Merrill Lynch prospectus. This very argument was rejected in Marchetti v. United States, supra, where the Supreme Court noted the incongruity of the Government's assertion that defendant had waived the privilege by failing to present it to the Treasury Department:

"...to have required him to present his claim to Treasury officers would have obliged him 'to prove guilt to avoid admitting it.' In these circumstances, we cannot conclude that his failure to assert the privilege to Treasury officials at the moment the tax payments were due irretrievably abandoned his constitutional protection. Petitioner is under a sentence for violation of statutory requirements which he consistently asserted at and after trial to be unconstitutional; no more can here be required."

--390 at 50-51
(citations omitted)

The Evidence Relating to the Purchase
of Stock for UBCJA Officials Should
Not Have Been Admitted at Trial

The Government maintains that the trial court properly retained the specification charging payments to UBCJA officials (paragraph 16) because the language of that paragraph, as redacted, was not inflammatory, and also because the specification was relevant to the securities law and mail fraud charges (GB, pp. 85-88). The first contention is really superfluous, since defendants never claimed error with respect to the redacted language of paragraph 16. However, the Government's support for the latter contention -- "in light of the obvious importance of unions. . . the relevance is obvious" (GB, pp. 87) -- does not even begin to meet the issue raised by defendants.

No evidence was ever offered to show that Homex's labor relations were influenced by the purchases of stock for union officials. Indeed, such payments were certainly never shown to have secured harmonious labor relations, and no Homex filing ever represented that harmonious labor relations would continue. Thus, the charge that the failure to disclose these payments violated the securities law and mail fraud statutes was never proven. See United States v. Koenig, 388 F. Supp. 670, 704-05 (S.D.N.Y. 1974).

Furthermore, the very nature of this charge set it apart from the balance of the specifications, all of which related to Homex's earnings. The gravamen of paragraph 16 was that Homex had paid off union officials, a charge that would have had a tremendous impact on the jury even if Homex had been a privately-held corporation incapable of violating the securities law. Additionally, the

Government's presentation of the case did not include any attempts to demonstrate a corrupt relationship between Homex and the UBCJA, and only focused upon the fact that purchases of stock had been made for the UBCJA officials. The larger perspective which the Government claims in this Court -- that the pay-offs were part of a scheme to defraud Homex investors -- was not even suggested to the jury in the Government's closing arguments.

The problem of confusion and prejudice presented by the labor union issue was palpable, and should have led to its exclusion prior to trial. As Mr. Justice Cardozo noted in Shepard v. United States, 290 U.S. 96, 104 (1933), "When the risk of confusion is so great as to upset the advantage [of its admission], the evidence goes out." The labor union issue was never properly a part of the securities fraud case, and only served to demonstrate that defendants were not above the performance of criminal acts.

II

WILLIAM STIRLING'S MOTION FOR A JUDGMENT
OF ACQUITTAL SHOULD HAVE BEEN GRANTED, OR,
ALTERNATIVELY, HE SHOULD BE GRANTED A NEW
TRIAL BY REASON OF THE GOVERNMENT'S INFLAM-
MATORY REBUTTAL SUMMATION
(Replying to Point III of the Government's Brief)

The Government's review of the evidence against William Stirling (GB, pp. 90-94) is basically a re-run of its rebuttal summation (A 555a-h), and unfortunately bears little relationship to the evidence it cites.

The Government's principal argument is that William Stirling "must be seen in the context of his responsibilities at

Homex [as] President of the Company, chief operating officer, and a director." (GB, p. 90). This fact, standing alone, does not create any inference of guilt. See, e.g., United States v. Danser, 26 F.R.D. 580, 586 (D. Mass. 1959) (Wyzanski, J.). Moreover, it ignores the obvious fact that William Stirling was at all times subordinate to his elder brother, and that all of his alleged activities were more likely the result of brotherly trust than a desire to defraud. An examination of the evidence cited against William indicates few acts which were done independently of his brother.* Equally important, the activities which the Government points to are, on any reasonable view of the evidence, greatly overstated.

Thus, the Government asserts that "[William's] frequent attendance at the meetings of [the finance and executive] committees shows his active leadership in the affairs of the business." (GB, p. 90). This statement is based solely upon Homex's corporate minutes, which themselves show that he was essentially a bystander who never proposed, seconded or discussed any act complained of in the indictment or bill of particulars. Indeed, the Government essentially concedes that William Stirling was a mere attendee by its failure to point to even a single instance where he "actively led" Homex into anything.

*By way of example, we would note that the Government's final piece of "evidence" against this defendant is David Stirling's having offered the use of Mrs. William Stirling's car to McCann "to escape a subpoena from [Homex's] trustee in bankruptcy" which was never issued (GB, p. 93). Although this charge is not probative of anything, its inclusion in the Government brief (as in its closing argument [A 556h]) indicates the weakness of the case against William Stirling.

Similarly, the Government's assertion that William Stirling "strictly controlled" Homex's public relations (GB, p. 90) rests solely upon prosecution witness Levering's statement that annual reports, press releases, and other corporate communications could not be released without William's approval. A fair presentation of Levering's testimony would also note that he could not point to even a single instance in which William Stirling had suggested, vetoed, or made a substantive contribution to any of these documents.*

The balance of the Government's charges against William Stirling are equally inflated. His participation in the land sales boiled down to the fact that William, along with his brother, had transferred interests in limited partnerships to Peter Thun at the same time that Thun was paying Kece's mortgage (GB, pp. 91-92). Putting aside the fact that Thun never

*Indeed, the only change in Homex's 1971 annual report which Levering attributed to William Stirling was changing the word "produce" to "product" (Tr. 2778-79). Moreover, Levering also testified that William Stirling did not write the financial portion of the report, and did not even receive the background memorandum from which it was derived (Tr. 2792-93).

The Government, in attempting to bolster William Stirling's role, also suggests that he collected the copies of the first draft of the 1971 annual report to cover up "a patent indication of Homex's financial weakness", a \$3.8 million tax refund (GB, pp. 90-91). This charge is belied by Levering's testimony that Shea Gould, Homex's outside counsel, had ordered the deletion (Tr. 2808-09). Rather than set the record straight, the Government compounds its error by asserting that "The final version of the report [was] done under William Stirling's careful supervision" -- despite the fact that Levering suggested that everyone but William Stirling worked on the annual report (Tr. 2792-93, 2805-07).

testified to any meetings with William in regard to any part of the Kece transaction, the Government's claims are squarely contradicted by the testimony of its own witnesses. See pp. 8-9, supra.* Similarly, the evidence supporting William Stirling's depiction as Homex's "censor" by "controlling the flow of information" to Merrill Lynch and its counsel (GB, p. 92) consists solely of an "O.K." in response to the question of whether it was "O.K. to mail" them the information they had requested (E 487). Likewise, "the failure to release news" relating to Greater Gulf can hardly be attributed to William Stirling, since Levering himself testified that Carl Wren, a Homex Vice-President, had total control of the publicity relating to Greater Gulf and that William Stirling had not even been advised of Wren's public relations campaign in Mississippi (Tr. 2750, 2787-88).**

The evidence relating to William Stirling's role in the labor stock transactions is even less substantial. The testimony cited for "William Stirling directly approached Ruggiano and urged him to buy the stock in Homex" (GB, p. 93) --

*Curiously, the Government's treatment of the Mobil Towns transactions totally ignores the prosecution's blatant misstatement of Thun's testimony regarding the source of the Kece payment in his summation. See St. Br., p. 21; compare A 396 with A 555-56. Likewise, the Government claims that the Stirlings sold their interest in Hollyrood Park Associates "in return for" Thun's execution of a PMM confirmation, even though Thun testified that "nothing was given to him by way of special treatment or anything by Homex or the Stirlings to . . . sign the confirmation" (Tr. 3203).

**The Government's suggestion that William Stirling's "policy" was "to bury or omit entirely financial information such as the gigantic [Greater Gulf] \$100 million backlog" is grossly misleading. The "backlog" information, suggested by Levering himself, was only omitted from the press release, but was put in the "fact sheet" released at the same time (Tr. 2265-68).

conversations which Ruggiano himself described as "limited discussions with both [Stirlings] going through the hall" (Tr. 581) -- simply does not support the Government's characterization:

"Q Who offered you the stock?

'A Well, Frank Csapo.

'Q Do you remember the circumstances of it?

'A No, I don't remember. Also Bill Stirling and David Stirling

'Q You were all together?

'A At different times they made mention of stock; that it was going to be a good thing and go up and stuff like that, and I ought to buy in the stock, and I said, "I don't know if I can or not. I don't know if it is legal. 'Oh', he says, 'there is no question about it. We'll check with out [sic] attorney.'"

'Q Who was that attorney -- Yanowitch?

'A Yes, Yanowitch.

'Q What did Yanowitch say?

'A I don't know. I never talked to Yanowitch, but they told me it was perfectly legal."

(Tr. 581-82)*

As its final argument, the Government claims that William Stirling -- with the assistance of his wife's automobile -- "betrayed his guilty knowledge of his past behavior by actively joining in the cover-up" after he had left Homex (Ct. B, p. 93). A more candid description of such activities would also refer to the fact that shortly before they left Homex, the

*The additional assertion that William Stirling "also joined in submitting the false travel expense vouchers [to pay the UBCJA loans]" is likewise misdirected, since the Government pointedly fails to note (though raised in Stirlings' Brief at p. 56) that the voucher attributed to this defendant was never authenticated, and, as is apparent on its face, was never signed by William Stirling. Compare E 432 with E 487.

Stirling brothers had been named as defendants in class actions claiming damages of more than \$30 million. Furthermore, the "active" participation to which the Government refers relates to William's presence in his own home and his removal of personal papers from his former office at Homex.*

In sum, the evidence against William Stirling did not justify denial of his motion for a judgment of acquittal. Unlike the decisions referred to by the Government (GB, p. 94), there was no direct or circumstantial evidence of William Stirling's knowing participation in a scheme to defraud.** Moreover, the case against William Stirling presents one fact which is totally foreign to the usual conspiracy case: while most conspiracy cases involve unrelated parties joined together for common financial benefit, William is the younger brother of the alleged head of the conspiracy and more likely to have been acting because of brotherly trust than a conspiratorial

*Significantly, McCann did not testify to any conversation with William Stirling, and no witness ever claimed that this defendant had removed anything other than his personal papers from his Homex office.

**The Government's reliance upon United States v. Hanlon, 548 F.2d 1096 (2d Cir. 1977) is ill-advised, since the "personal" typing which Katritsis performed for Amanatides would have informed him of Amanatides' criminal scheme. Likewise, in United States v. Marrapese, 486 F.2d 918 (2d Cir. 1973), cert. denied 415 U.S. 994 (1974), the defendant's sole contribution to the incriminating conversation -- "He wants to buy the rifles?" -- was sufficient to establish his knowledge of the scheme to sell stolen machine guns. Significantly, the Government fails to point to even a single shred of evidence which indicates William Stirling's awareness of the alleged scheme to defraud.

agreement. The element of criminal motivation simply cannot be presumed in these circumstances, especially where the evidence of knowing participation is so insubstantial as to be non-existent.

Moreover, since the Government had at best a very weak case against William Stirling -- a fact which the trial court itself recognized (A 427) -- the inflammatory nature of the Government's rebuttal summation was especially prejudicial. Inasmuch as the Government has not responded to the points initially raised with respect to this summation (St. Br., pp. 53-58), we shall only deal with three of the more salient misstatements the Government makes in claiming that "each challenged prosecutorial comment was fair." (GB, p. 95)*

The Government thus characterizes, as "fair comment", the prosecutor's "point[ing] out to the jury the omissions from Homex's movie ['It Can Be Done'] (GB, p. 96). It is incredible that the Government can maintain, at this late date, that a 20-minute documentary should have given a full description of Homex's financial condition, and at the same time claim that it "never contended that the movie was a registration statement". (Ibid.) It is even more incredible that such "misuse" of the "It Can Be Done" was attributed to William Stirling, whose only connection with the film was his approval of Levering's program for making it. (Tr. 2749)

*In particular, the Government has responded to none of the prosecutor's misstatements referred to at page 56 of the Stirlings' Brief.

Likewise, the Government's characterization of Ruggiano's testimony -- itself twice the length of the testimony cited (compare GB pp. 96-97 with Tr. 581-82 [quoted at p. , supra]) -- reads far too much into Ruggiano's "limited discussions . . . going through the hall". Moreover, it pointedly ignores the ambiguity in Ruggiano's testimony as to both the source of the alleged "urging" -- Csapo, David Stirling, or William Stirling -- as well as what would be illegal about the purchase -- placement on the original issue list or purchases on the open market.* The "clear thrust of Ruggiano's testimony" to which the Government refers (GB, p. 97) simply is not there.

Finally, the Government asserts the reference to the "open question . . . as to how much more money really was being taken out through the expense accounts" (A 556g) was justified as "fair rebuttal" to David Stirling's testimony that he and his brother "were content with the money they had and were not looking for more . . ." (GB, p. 97). This argument is not supported by the Government's citations, which principally refer to David Stirling's testimony that both he and his brother believed in Homex's future, wanted to hold on to as much of their Homex stock as possible, and were not

*The Government mistakenly claims that "of course, it was not [legal]", without attempting to explain the type of purchase to which it refers (GB, p. 96). Significantly, no UBCJA official was ever placed on Homex's original issue list, and Langone himself testified that purchases in the after-market by UBCJA officials were perfectly proper (Tr. 347-48, 376-77).

interested in selling the company to General Electric, Bethlehem Steel, or other corporations which wanted to acquire it. See Tr. 4029, 4087-90. Likewise, contrary to the summation's characterization of the Stirlings' closing argument, there was no contention that they "didn't take very much in the way of money out of this company." (A 556f; cf. Tr. 3955, 5655) The claim of "fair rebuttal" is hardly descriptive of this type of cheap shot, which raised a new charge never alleged in the indictment or the bill of particulars and certainly never proven at trial.*

III

THE TRIAL COURT DEPRIVED DEFENDANTS OF A
FAIR TRIAL BY REASON OF ITS EXCLUSION OF
DEFENSE WITNESSES WIND AND TURZIK AND ITS
LIMITATION OF CROSS-EXAMINATION OF PROSECUTION WITNESSES

(Replying to Point VII of the Government's Brief)

In attempting to minimize the prejudice resulting from the trial court's exclusion of defense witnesses Daniel Wind and Peter Turzik and its limitation of cross-examination, the Government misstates defendants' arguments and assumes, in this Court, a posture totally dissimilar from their position at trial.

*The Government claims that this "open question" was justified by GX 856, a memorandum prepared by Dienstag concerning changes to be made in the 1971 proxy statement. Contrary to the Government's statement that the Stirlings and Yanowitch "were drawing well in excess of their salaries in the fall of 1971", Dienstag wrote that they had drawn more than the existing "contract figures". Pursuant to Dienstag's memo, new contracts were drawn up and the full amount of defendants' drawings were disclosed in the proxy statement. Thus, the "open question" to which the prosecutor referred was never an issue at trial. Indeed, if the Government had fairly presented GX 856, it would have confirmed defendants' claim that in all SEC matters, they relied on the advice of Kramer and Dienstag and always followed their recommendation.

Thus, with respect to the exclusion of Wind, the Government asserts that such testimony was irrelevant because "the jury was repeatedly told in the Government's summation that Homex had made numerous genuine sales", and defendants were only being tried for "the criminal excesses" (GB, p. 118). Apparently, the author of this sentence did not read the opening line of the Government's statement of facts, claiming that Homex "from beginning to end, was a massive fraud conceived and executed by defendants. . ." (GB, p. 3). Wind's testimony -- that the State of Israel was ready, willing and able to make an immediate purchase of \$2.5 million -- would have greatly dispelled the Government's claim that, at the time of defendants' departure, Homex was moribund.* The testimony relating to this sale would have lent credence to defendants' claim -- firmly denied by the Government throughout this trial -- that Homex was a viable company until the banks, having bailed themselves out with the proceeds of the Merrill Lynch offering, took the money and ran. It was certainly not too much to ask that defendants, saddled with the stigma of Homex's bankruptcy, be permitted to show the grounds for their sincere belief in Homex's future. See, e.g., Frank v. United States, 220 F.2d 559 (10th Cir. 1955) (Securities Act conviction vacated where,

*Such testimony would have also substantially undercut the Government's allegation that Homex's reassignment of modules was fraudulent (Indictment, ¶14), since the sale to Israel vividly demonstrated that modules were legitimately reassigned because of unanticipated sales to new customers.

inter alia, court excluded statements tending to show defendant's good faith); cf. Getchell v. United States, 282 F. 2d 681 (5th Cir. 1960).*

The Government's defense of the exclusion of Peter Turzik is neither persuasive nor candid. Throughout his direct testimony, David Stirling had taken the position that Kheel knew all along that UBCJA officials were going to purchase stock in Homex and, as a Homex director and its labor relations counsel, had never objected to their inclusion. See, e.g., A 451-53. When Kheel was called as a rebuttal witness, he testified that he had not designated any UBCJA officials for Homex's original issue list and did not know that UBCJA officials had bought stock in the company (A 479-82). Turzik, a UBCJA official would have given the lie to both these claims, since his purchase of Homex stock had been arranged by Kheel himself (A 494).

The Government now claims that the exclusion of Turzik was proper because "he was not one of the seven UBCJA officials charged in the indictment and his name had not appeared on the David Stirling loan guarantee letter" (GB, p. 119).** This argu-

* The Government attempts to play down the impact of Wind's proposed testimony by suggesting that prosecution witness Dienstag's memorandum (GX 612), which implied that Homex was no longer viable, had already been rebutted by defense witness Newman Evans. However, the Government's own characterization of Evans as a "current Stirling aid" only serves to emphasize the importance of a totally impartial witness such as Wind. (GB, p. 118).

**For some reason, the Government attributes the trial court's ruling to the fact the testimony "did not go beyond a desire to contradict Kheel's earlier answer that he had not arranged for Homex stock 'from' Mr. Turzik" (GB, p. 120, citing Tr. 5453). Rather than rely on the Government's characterization, we invite the Court's attention to the ruling itself, which did not posit any such limited purpose.

ment is spurious: if Kheel had been shown to have been aware of Turzik's placement on Homex's original issue list -- let alone having arranged it himself -- it would have supported David Stirling's claim that he had relied upon Kheel's advice (Tr. 4120-21). Moreover, since Kheel had written the "Labor Relations" section of Homex's SEC filings, Turzik's testimony would have lent strong support to defendants' claim that the SEC filings had been the responsibility of outside professionals fully familiar with all of the facts (Tr. 5400-01; cf. Tr. 4161-62). The Government's attempt to separate Turzik from the seven other UBCJA officials is unconscionable, since the basic issue was Kheel's knowledge of the UBCJA purchases which were not disclosed in the registration statement he himself had prepared. For this purpose, it made absolutely no difference that Turzik was not listed in paragraph 16 of the indictment.*

Finally, the Government understates defendants' contentions with respect to the trial court's admonition against counsel's use of "were usual"/"were unusual" questions. To be sure, the use of such questions would have been helpful

*Moreover, the Government's closing summation unfairly emphasized the fact that defendants had been unable to link Kheel to any UBJCA official. The prosecutor's summation, in arguing that Joseph Lane Kirkland's involvement with Kheel was irrelevant, distinguished his participation only because he was not a UBJCA official. See A 552-53. Indeed, this was the only point the Government sought to establish in Kirkland's two-question cross-examination (A 500). It is obvious that the Government would never have attempted this type of argument if the jury had heard that, in addition to the seven UBCJA officials named in the indictment, an eighth -- Turzik -- had been put into Homex by Theodore Kheel. It ill-behooves the Government, having unfairly capitalized on Turzik's exclusion, to now assert that his testimony was in any sense collateral.

in permitting counsel to demonstrate the bona fides of Homex's involvement with Greater Gulf. However, the real vice of the trial court's ruling -- which it noted in stating that "if this is erroneous it is not harmless [error]" (A 324) -- was its effect on the balance of defendants' cross-examination of prosecution witnesses. As the Government itself notes, defense counsel had previously asked similar questions of other Government witnesses, and the trial court had instructed them to desist (GB, p. 117). The direction complained of was the last one given to defense counsel, and no such further questions were asked. This limitation was prejudicial because this was a highly technical case, and such questions would have materially augmented the jury's understanding of the issues involved. Indeed, after this final direction, prosecution witnesses testified on such topics as banking and FHA procedures (Marshall), real estate closings (Bartz), auditing (Kesel), accounting (Mauriello, Murray), public relations (Levering), and SEC practice (Dienstag). We submit that the learned trial judge perceived the full impact of his ruling far better than the Government, and properly acknowledged that he was materially weakening defendants' ability to cross-examine. The blanket ruling, in a case of this type, was prejudicial error depriving defendants of a fair trial.

IV

DEFENDANTS ARE ENTITLED TO A NEW TRIAL BY
REASON OF THE PREJUDICIAL AND ERRONEOUS
CHARGE TO THE JURY
(Replying to Points I and VI of the Government's Brief)

Defendants incorporate by reference the arguments set forth in the Yanowitch Reply Brief at pp. 17-32.

V

THE STIRLINGS WERE DEPRIVED OF DUE PROCESS
OF LAW BY REASON OF THE GOVERNMENT'S USE OF
DAVID STIRLING'S ADMISSION OF TAFT-HARTLEY
VIOLATIONS MADE IN CONNECTION WITH A GUILTY
PLEA VACATED BECAUSE OF THE GOVERNMENT'S
FAILURE TO PRODUCE EXCULPATORY EVIDENCE

By motion filed in this Court on July 18, 1977, the Stirlings and Yanowitch have moved to remand this appeal for a hearing in the District Court of their claim that the trial court improperly permitted the Government to use admissions made by David Stirling and Yanowitch in connection with their pleas to a Taft-Hartley Act indictment in the Western District of New York. While this appeal was pending, Judge Harold P. Burke, by order dated July 12, 1977, vacated the pleas upon the ground that the Government had violated Brady v. Maryland, 373 U.S. 83 (1963).

At the present time, the motion for remand is still pending. By separate motion, also filed on July 18, 1977, Yanowitch and the Stirlings have requested permission to file supplemental briefs in this Court in the event that the Court declines to remand the case.

In the event that this Court declines both a remand and an opportunity to submit further briefs, the Stirlings respectfully request that the Court deem the papers submitted on the remand motion, in which both the Government and appellants discuss the merits of this claim, as part of the briefs filed herein.

CONCLUSION

The judgments of conviction against David Stirling, Jr. and William G. Stirling should be vacated, and the indictments dismissed or, in the alternative, a new trial ordered.

Dated: New York, New York
August 10, 1977

Respectfully submitted,

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STATE OF NEW YORK)
 : SS.:
COUNTY OF NEW YORK)

ELIZABETH PEPE, being duly sworn, deposes and says that she is not a party to this action, is over 18 years of age and resides at 4320 Forman Avenue, Bronx, New York, 10466. That on the 10th day of August, 1977, deponent served the within Reply Brief of Defendants-Appellants David Stirling, Jr. and William Stirling and the Reply Brief of Defendant-Appellant Harold M. Yanowitch upon

Douglas F. Eaton, Esq.
Suite 1905
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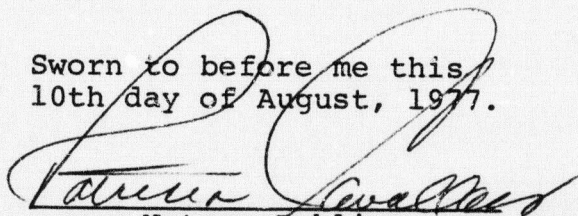
-and-

Patterson, Belknap & Webb
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New York, New York 10020

attorneys for defendants William Schulz and Rubel Phillips, respectively, by depositing two copies each of same enclosed in a post-paid properly addressed wrapper, in an official depository under the exclusive care and custody of the United States Postal Service within the State of New York.


ELIZABETH PEPE

Sworn to before me this
10th day of August, 1977.


Notary Public

PATRICIA CAVALLARO
Notary Public, State of New York
No. 24-4501005
Qualified in Kings County
Commission Expires March 30, 1979

2
COPY RECEIVED
AUG 10 1977
U. S. ATTORNEY
SO. DIST. OF N. Y.
ROBERT B. FISKE JR.

